



NORTH AMERICAN CAPITAL APPRECIATION STRATEGY

Third Quarter Review

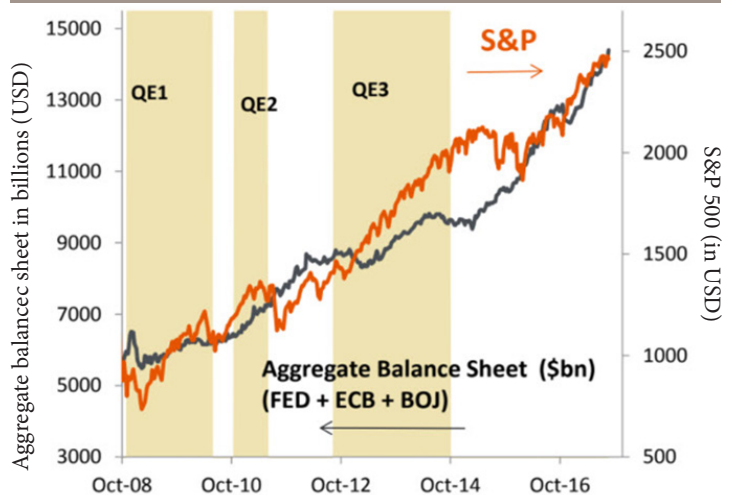
September 30th 2017

Even though the economies north and south of the border continue to muddle along, some economists are describing the current environment, particularly in the US, as one of the best in a long time. The combination of synchronized global economic growth, low inflation, a reasonably accommodative central bank and rising corporate earnings are quite a powerful combination that could keep this market going for a while yet. The final reading for US second quarter GDP ticked up to 3.1% from 3.0%. This would normally suggest a reasonably strong hand-off for the back half of 2017, although we may see a hit in the third quarter due to missing output caused by hurricanes Irma and Harvey. This may cause a bigger rebound in the fourth quarter as rebuilding and spending on reconstruction takes place. US employment growth, also likely to be muted somewhat in the coming report due to the hurricanes, overall continues to impress with the unemployment rate of 4.4% still close to a 16 year low. Meanwhile on the inflation front, in our last quarterly commentary we talked about how powerful secular forces may be keeping wage demands in check in spite of a tighter labour market. These forces include competition resulting from globalization, deflationary technological innovations and demographic drag from aging populations. And then of course, there is Amazon that is doing its best to lower prices on everything in its path with the latest being organic healthier food.

The US Federal Reserve (Fed), while holding rates steady at its September meeting, indicated one more hike by year end and is targeting three in 2018. They view the current low level of inflation as transitory as the labour market continues to strengthen and economic activity

is rising moderately. We did see the US consumer price index (CPI) tick-up in August to 1.9% from 1.7% in July so while low, directionally we would agree the next move is likely higher. The lower US dollar and recent strength in commodity prices should also help fuel inflationary forces. Finally, the Fed also announced it will begin winding down its \$4.3 trillion crisis-era balance sheet starting in October. Exhibit 1 shows the impact on the S&P500 price performance since 2008 when the Fed, the European Central Bank (ECB) and the Bank of Japan introduced quantitative easing.

Exhibit 1
Central Bank Balance Sheets vs. S&P 500



Source: Bloomberg, PiperJaffray, WSJ

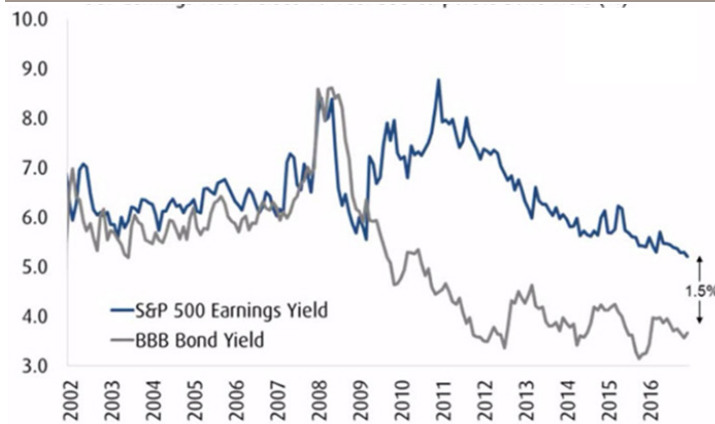
So the concern is that with the Fed beginning the wind down of global quantitative easing, will this mark the end of the bull market? The answer is we really don't know for sure; however, the initial dollar amount of the wind down is small, the pace appears to be fairly



gradual and the Fed's monetary stance overall is still fairly accommodative. Intuitively it could put upward pressure on the long end of the yield curve and only time will tell how much pressure. This is not necessarily a bad thing, particularly if you own financial stocks that generally benefit from a steepening yield curve.

Exhibit 2 shows the positive correlation between earnings yield on stocks (earnings divided by price) and investment grade corporate bond yields going back 15 years. This supports the idea that the S&P500 is not expensive relative to the low level of bond yields and there is room for earnings yields to move higher with earnings growth without causing prices to fall or conversely, there is room for earnings yields to move lower as prices rise.

Exhibit 2
S&P Earnings Yield versus 10-Year BBB Corporate Bond Yield (%)



Source: Standard & Poor's, BMO Private Bank Strategy, WSJ

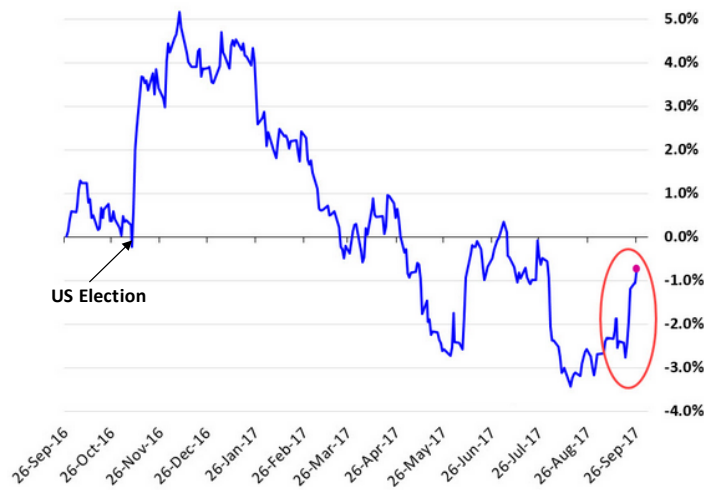
In Canada, one can't help but feel our central bank governor has done a bit of a flip – flop after raising rates twice, once in July and again in September. Our central bank's rationale was based on the better than expected broader-based economic growth as well as a stronger consumer underpinned by continuing employment and income growth. With second quarter GDP running at an

annualized pace of 4.5%, although slowing slightly in July to 3.8%, this was seen as justification for eliminating the two emergency 2015 rate cuts. Meanwhile in a speech last week, Governor Poloz said there is no predetermined path for rate increases and the Bank of Canada will proceed cautiously on further rate hikes. He noted concern about how high household debt levels amplify the impact of any tightening and that ongoing wage growth was not keeping pace with GDP growth. This has resulted in a roller coaster ride for our Canadian dollar, which started the quarter at US \$0.77 and peaked shortly after the second rate hike in September at US\$0.82 and has since fallen back to US\$0.80. Unless oil prices continue to rise significantly from here, which we don't believe is likely barring some exogenous shock and with the Bank of Canada moving to the sidelines on rate hikes, we don't expect much further upside for the Canadian dollar from here.

Finally, we should touch on what is happening in Washington before getting into detail about the quarter. Our Chairman did a good job at our September client quarterly meeting in describing the North Korea situation and tying in how much expectations are built into the market for the Trump administration economic agenda. The short answer is a decline of as much as 8% or 9% to get back to the same P/E multiple of just over 16x the S&P500 at the time of last year's U.S. election. However, when we look at what the Trump administration has accomplished so far not much has happened. Not much deregulation, not much infrastructure spend, no tax reform and no tax break on foreign cash holdings repatriated back to the US (although the last two seem to be back on the agenda). Exhibit 3 shows the share price impact on a basket of high corporate tax paying companies relative to the S&P500 post the election of president Trump.



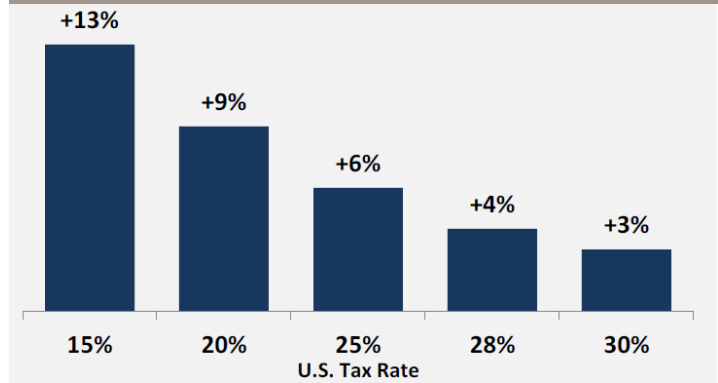
Exhibit 3
GS High Tax Rate Basket- S&P 500 Index: Relative Performance



Source: WSJ

As indicated in the chart, while there was a quick increase in the price of these stocks in the first couple of months post the election, this now appears to have completely unwound suggesting the residual (8%-9%) upward movement in the S&P500 since the election may be related to other factors. Lately we have seen a price recovery in this high tax basket over the GOP's refocus on tax reform. Exhibit 4 shows the impact on the S&P500 earnings under different possible taxation scenarios of tax reform. The talk right now is centred around a reduction from the marginal rate of 35% for corporations to 20%. That alone could be material adding 9% to 2018 and 2019 earnings not to mention any further impact from repatriation of cash.

Exhibit 4
S&P 500 EPS Impact at U.S. Corporate Tax Rates



Source: WolfeResearch, WSJ

The Bloomberg consensus outlook for earnings in 2018 and 2019 is \$145.1 and \$159.9, respectively, or 11.1% and 10.2% growth over the \$130.7 2017 earnings base. However, if tax reform were to happen, we think consensus earnings would be even higher such that the S&P500 could be trading at 15.9x and 14.5x 2018 and 2019, respectively, versus forward estimates today of 17.8x. While this is not a forecast, it does provide a clear understanding of why the market could go a fair bit higher here from higher earnings revisions or multiple expansion (lower earnings yield).

During the third quarter of 2017, the S&P500 Index was up 4.5% in US dollars. Adjusting for currency, the S&P500 returned 0.5% in Canadian dollars, as the Canadian dollar appreciated about 4%, closing the quarter at US\$0.80. Year to date the S&P500 returned 14.2% in US dollars and 6.2% in Canadian dollars. In Canada, the TSX returns in the third quarter and year to date were 3.7% and 4.5%, respectively. While Canadian equities have underperformed relative to US equities year to date in 2017, the performance in the third quarter has improved and exceeded the S&P500 on a currency-adjusted basis.

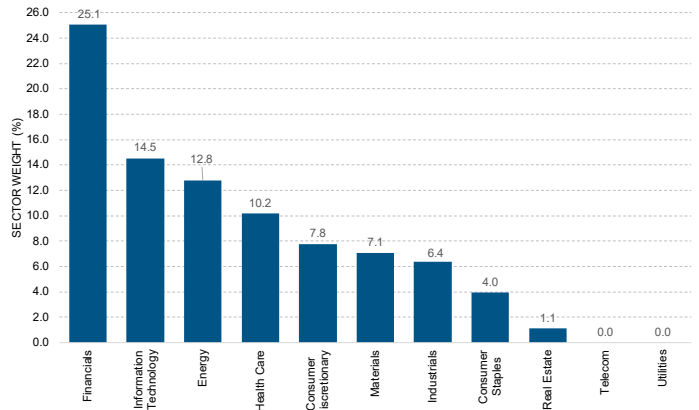


Asset Allocation for our North American Capital
Appreciation Strategy
As at September 30, 2017

Equities	88%
Fixed Income	8%
Cash	4%

During the third quarter, our asset mix continued to shift slightly in favour of Canada versus the US as our Canadian equity weight increased another 2% to 44% after a 5% increase in the second quarter, while our US equity weight declined slightly from 45% to 44% such that the overall equity exposure grew slightly 87% to 88%. Valuations in Canada continue to look more attractive overall than the US but with slightly less earnings growth than south of the border. So, we have been very company specific in adding to existing positions in IGM financial and CGI Group, and initiating a new position in National Bank of Canada. Both IGM Financial and CGI Group are seeing a strong acceleration in earnings growth. In the case of IGM due to improving mutual sales and higher operating leverage as heavy spending on digital technology and branding is curtailed. CGI Group is expected to benefit from the acceleration in the global digital transformation of businesses that need to stay competitive and relevant. Big data, automation and digitization remains a theme that's relevant to our large exposure in Information Technology (Exhibit 5). Our other large sector exposure is Financials and we added National Bank of Canada and Discover Financials Services.

Exhibit 5
Sector Allocation
September 30, 2017



Source: Cumberland Private Wealth Management

National Bank conducts most of its business in the “no boom no bust” province of Quebec, which has not experienced the run up in residential housing prices that we have seen in other parts of Canada. At the time of purchase, it traded slightly over 10x earnings and has the highest return on equity (ROE) and strongest capital ratios of all the banks in Canada. Discover Financial services is a consumer bank in the US trading at a sub 10x P/E multiple. With an ROE of 19% and a 37% tax rate, this bank is very profitable and would also be a major beneficiary of tax reform in the US. Both companies would also benefit from higher interest rates. We also added Hanesbrands and Kohl’s Corp. in the US consumer discretionary sector. These stocks were attractive from a contrarian perspective as both have been impacted negatively by the shift to online retailing versus traditional bricks and mortar. Hanesbrands Inc. suffered a major inventory correction as its largest customers retrenched to deal with this shift and it reoriented itself towards online retailing. Kohl’s simply got too cheap, trading close to its



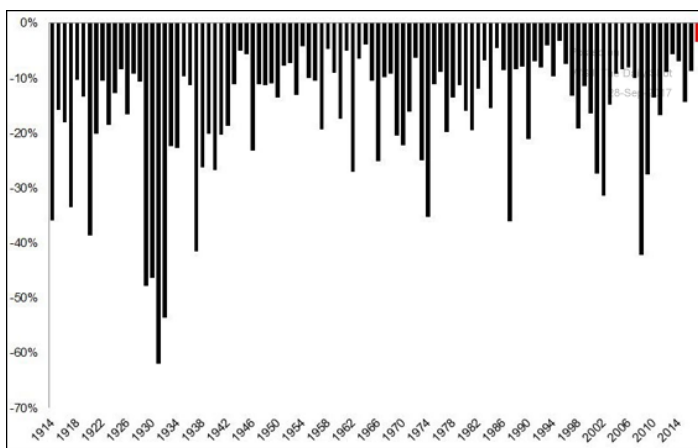
real estate value with very little value left for its profitable retail franchise. Kohl's has since partnered with Amazon which has been a positive development for the stock.

The other change to note is our Fixed Income weight has increased to 8% from 4%. The majority of the shift is due to our investment in the Cumberland Short Term Bond Fund, which carries a very short duration of less than 3 years. We believe it will earn a much better risk-adjusted return versus holding cash or near cash investments, and it will also help dampen the volatility of the portfolio in the event of a pull-back in equities. A complete summary of new positions added during the quarter, including business fundamentals and valuation metrics, is contained in Appendix 1.

Outlook

Exhibit 6 shows the maximum drawdown by year for the S&P500 going back to 1914. As indicated in the chart, the S&P500 has had the lowest maximum drawdown on record so far in 2017.

Exhibit 6
Maximum Drawdown in the S&P 500 Each Year



Source: Reformed Broker, Michael Batnick, WSJ

Cumberland Private Wealth Management Inc. is a leading independent investment firm that provides discretionary investment management and wealth management services for high net worth individuals, their families and foundations, with \$1 million or more in investable assets. All of Cumberland's investment mandates are centered on building and preserving our clients' financial wealth. Founded in 1997, the firm is privately-owned by its employees and headquartered in Toronto, Canada.

This in itself may be reason to expect some type of short term pullback but overall, the outlook for economic growth in both North American economies and for earnings in general remain very positive. So we maintain a net positive bias on the outlook for the North American equity markets and that explains our equal equity balance currently between the US and Canada. The S&P500 is trading at 17.4x and 15.8x 2018 and 2019 respective earnings, which is not particularly cheap; however, the outlook for earnings growth in both years remains double digit (11.1% and 10.2%, respectively) and we don't believe there is much built into these estimates in the event of Trump tax reform or other fiscal measures that could stimulate growth. In Canada, the TSX is cheaper trading at 16.0x and 14.4x 2018 and 2019 earnings respectively, also with close to double digit earnings growth expectations (9.8% and 11.4%, respectively) looking out to 2018 and 2019. Earlier we highlighted the current level of earnings yield for the S&P500 relative to 10 year investment grade corporate bond yields implying that in an accommodative low interest rate, low inflationary environment, there is room for S&P500 earnings multiples to stay elevated and the environment in Canada is currently no different. Given the current outlook for economic growth is positive with the likelihood of a recession very low, we continue to believe equity markets will likely grind higher from current levels.

Peter Jackson
Chief Investment Officer
October 1, 2017



APPENDIX 1

NEW EQUITY INVESTMENTS:

CUMBERLAND NORTH AMERICAN CAPITAL APPRECIATION MANDATE

United States

Discover Financial Services (DFS)

Discover Financial operates a direct banking and payment services company in the United States. The Direct Banking segment offers Discover-branded credit cards to individuals; and other consumer products and services, including private student loans, personal loans, home equity loans, and other consumer lending, as well as deposit products, such as certificates of deposit, money market accounts, savings accounts, checking accounts, and individual retirement arrangement certificates of deposit. The Payment Services segment operates the Discover Network, which processes transactions for Discover-branded credit cards, and provides payment transaction processing and settlement services; and PULSE network, an electronic funds transfer network that provides financial institutions issuing debit cards on the PULSE network with access to automated teller machines and point-of-sale terminals.

We believe that the concerns over credit quality amongst credit card issuers are priced into shares. We believe the U.S. consumer is healthier than the market is pricing in today. Debt-to-disposable income remains well below 2008-09 levels suggesting room to move higher, and employment metrics all suggest a favorable consumer credit environment for the medium-term. DFS is well capitalized as a U.S. bank, and is projected to buyback approximately 8-9% of its outstanding shares over the next year. Valuation to the S&P500 and S&P500 banks remains very favorable to history.

Hanesbrands Inc. (HBI)

Hanesbrands Inc. (HBI) designs, manufactures, and sells basic apparel items around the world. They operate 52 manufacturing facilities, mostly in Asia, Central America, and the Caribbean Basin. HBI manufacturer's product for third parties as well, but is increasingly internalizing production where margins are much higher. We believe the company will continue to execute on its strategy of acquiring smaller brands and wrapping them into their manufacturing/design/distribution network.

We believe the market has been too pessimistic on the outlook for HBI. While sales in the past two years have been on the decline to a category shift from brick-and-mortar retail toward more online shopping, the period of inventory de-stocking by its major customers is slowly ending. We have a high degree of confidence in the defensibility of Hanesbrands' competitive position, given advantages that are difficult for competitors to replicate: the firm's large owned and controlled supply chain, core product positioning in a space where brand is more important than price, and economies of scale achieved through a growing portfolio of synergistic brands. HBI online sales via direct-to-consumer and through Amazon.com will be increasing to approximately 20% of total sales by 2019.

Our fundamental valuation work suggests upside to higher sales, continued cost synergies from past acquisitions and multiple expansion as the balance sheet de-levers over the next few years.

Kohl's (KSS)

Kohl's Corporation (KSS) a U.S. based department store that operates more than 1,100 stores in 49 states. They offer a range of exclusive, private-label and national brands in shoes, accessories, beauty, and home products.

Expectations for Kohl's are still quite low, as with other U.S. retail stocks, Kohl's shares have underperformed the S&P 500 over the last few years as the threat of Amazon.



com spread and the online retail disruption seemed to spell the end for all of retail. We see KSS as a self-help story for many reasons. The company is working to drive traffic into stores, reduce fixed costs and improve its inventory turnover. For instance, it will reduce costs by over \$250MM over the next 3 years. We believe operating margins will be sustained around 7-8% as a result, vs general expectations for sub-7% margins.

More recently, KSS has been pairing with Amazon.com via introducing an Amazon smart-home space inside Kohl's stores. Shoppers will be able to buy Amazon gadgets -- like Kindles and Fire tablets -- accessories and smart home products, such as the Echo speaker at these locations. This will result in increased foot traffic for Kohl's stores, it validates the brick-and-mortar approach to retail as even Amazon needs a physical presence to grow, and it provides KSS with a point of differentiation versus the department store peer group. Furthermore, under a trial period Kohl's stores will be accepting and processing merchandise returns for Amazon Prime customers at select stores. This further expands the partnership with Amazon which we believe is positive for Kohl's.

We believe that most of the bad news of retailing is now factored into valuation as shares trade at a considerable discount to department store peers and to the S&P500. KSS continues to buyback a substantial portion of its market capitalization, having bought back 50% of the outstanding shares in the last five years. We believe management and the board would consider taking the company private via a Leveraged Buyout strategy if the market continues to misprice KSS shares. This would yield considerable upside for us as shareholders.

Canada

National Bank of Canada (NA)

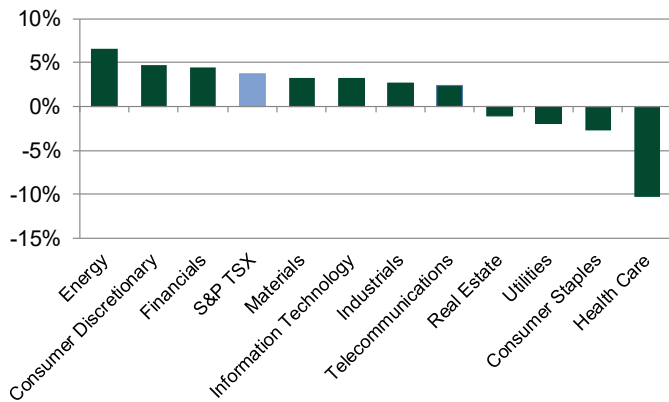
NA is one of the 'Big-Six' Canadian banks but it can be thought of as a Quebec & Eastern Canada regional bank. With assets of \$240 billion, it is half the size of its nearest 'Big Six' peer and, 60% of its \$6.2 billion annual revenues are earned in Quebec. That said, NA is currently delivering the highest returns on common equity amongst Canadian banks. We like NA for its concentration in Quebec and Eastern Canada, markets which we see as less vulnerable to oil prices and over-inflated house prices. NA is enjoying stable organic growth in its Personal & Commercial Banking and Wealth Management segments, reflecting Quebec's improving economic picture. Earnings growth is further enhanced by significant cost savings realized from the Bank's 2016 restructuring plan. Since its restructuring charges in 2016, NA has quickly rebuilt its capital level with its important common equity tier one (CET1) ratio reaching 11.2% in the most recent quarter. The improved profitability and peer-leading CET1 ratio suggests NA is likely to raise its dividend or increase share buy-backs in coming quarters. NA's shares trade at a discount to its Canadian banking peers despite its favorable earnings growth outlook and lower risk from oil and housing.



APPENDIX 2

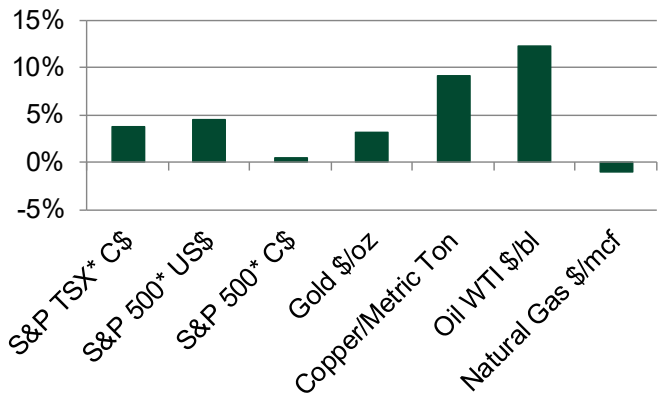
PERFORMANCE CHARTS

S&P TSX (C\$ Total Returns)
Quarter Ending September 30, 2017



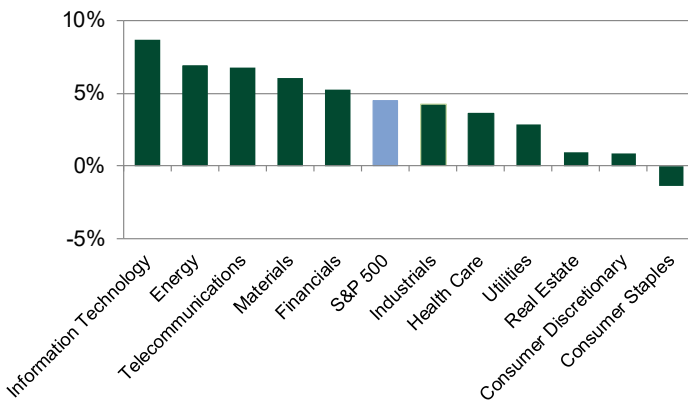
Source: TD Securities

Quarter % Change
Quarter Ending September 30, 2017



Source: Bloomberg *Total Returns

S&P 500 (US\$ Total Returns)
Quarter Ending September 30, 2017



Source: TD Securities